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Supreme Court of the United States

OCTOBER TERM, A. D. 1948.

No. _____.

UNITED FUNDS, INC., PETITIONER,

VS.

DAN M. NEE, UNITED STATES COLLECTOR OF INTERNAL REVENUE FOR THE SIXTH DISTRICT OF MISSOURI, RESPONDENT.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

To The Honorable, The Chief Justice, and Associate Justices of The Supreme Court of the United States:

Your petitioner, United Funds, Inc., respectfully prays that a writ of certiorari be issued to the United States Circuit Court of Appeals for the Eighth Circuit to review a judgment of that Court entered July 27, 1948 (169 F. 2d 33)*, reversing a judgment of the United States District

*Petition for rehearing denied August 18, 1948.

Court for the Western District of Missouri and directing a dismissal of petitioner's complaint. A certified transcript of the record in this case, including the proceedings in said United States Circuit Court of Appeals for the Eighth Circuit, is furnished herewith in accordance with Rule 38 of the rules of this Court.

STATEMENT OF MATTER INVOLVED.

United Funds, Inc., hereinafter referred to as Petitioner, was incorporated October 8, 1940, as a management open-end investment trust of the diversified type, with its principal place of business at Kansas City, Missouri (R. 3, 11, 13, 20, 21). In order to comply with the requirements of Section 80 a-17(f) of the Investment Advisers Act of 1940 (R. 139), Petitioner selected Commerce Trust Company as its Custodian and executed a "Trust Agreement" October 14 1940 (R. 62-88), providing for the transfer of all Petitioner's funds and its own Capital Stock to Custodian (R. 63); for the Custodian to collect and receive all income, profits, rights, etc. (R. 69); and for Custodian to pay for securities as they were ordered with Petitioner's funds in the Custodian's hands (R. 71). The Custodian then selected and registered a nominee in whose name all securities were issued (R. 122, 123) pursuant to a standing order to all brokers from Custodian (R. 124). When the securities were delivered they were paid for by the Custodian, with funds of the Petitioner in its custody (R. 22-23).

When securities were purchased, documentary stamp taxes were paid. However, following an examination and report by a revenue agent (R. 91-93), an assessment was made against Petitioner of additional stamp taxes for the period from November 12, 1940, to June 5, 1944, in the

amount of $5,849.95 (R. 90-93). The assessment was on the theory that Petitioner had transferred its right to receive securities (R. 4, 11), which transfers were subject to tax under Section 1802(b) of the Internal Revenue Code (R. 17). This amount was paid by taxpayer under protest (R. 105), and a claim was made for refund (R. 95). No action having been taken on the claim within six months of filing (R. 7-8, 12), Petitioner filed a complaint in the United States District Court for the Western District of Missouri on February 21, 1946 (R. 1, 3-8), to recover the tax paid with interest from the date of payment.

Defendant's answer (R. 9-12) was filed July 30, 1946, denying all material allegations in plaintiff's complaint.

Trial was had to the court and on June 18, 1948, the court entered its opinion and judgment* that Petitioner recover the tax paid with interest thereon from the time of payment (R. 13-18), finding that Petitioner had no right to receive the securities upon the transfer of which the tax was imposed; and that such a transfer, even if made, came within the specific exemption of Section 1802(b)(1) of the Internal Revenue Code (R. 7, 17).

The Government filed notice of appeal on September 15, 1947 (R. 19), and the cause was heard by the United States Circuit Court of Appeals for the Eighth Circuit. On July 27, 1948, the judgment of the District Court was reversed with directions to dismiss the complaint (R. 146-147).

On August 11, 1948, Petitioner filed its motion for rehearing (R. 148-156) and on August 18, 1948, Petitioner's petition for rehearing was denied (R. 157). On September 7, 1948, upon motion of Petitioner to stay the

*Reported in 72 F. Supp. 134.

mandate, the said Circuit Court of Appeals entered an order staying the issuance of the mandate for a period of thirty (30) days from and after that date (R. 158).

STATEMENT OF BASIS ON WHICH THE JURISDICTION OF THIS COURT IS INVOKED.

(a) Statutory Provisions Sustaining Jurisdiction.

The jurisdiction of this court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of June 7, 1934, Chapter 426, 48 Stat. 926 (28 U. S. C. A. 347*a*).

(b) The date of the judgment sought to be reviewed.

The judgment of the Circuit Court of Appeals reversing the judgment of the District Court was entered July 27, 1948 (R. 146-147), and Petitioner's petition for rehearing was denied on August 18, 1948 (R. 157). This petition for writ of certiorari and supporting certified transcript of the record were filed in this court within three (3) months from August 18, 1948.

THE QUESTIONS PRESENTED.

I.

Did the appointment by Petitioner of a Custodian as required by Section 80 a-17(f) of the Investment Advisers Act of 1940, and the Custodian's subsequent purchases of securities on behalf of Petitioner, constitute a taxable transfer of Petitioner's right to receive securities?

II.

If there was such a transfer of a right to receive, was it effected at a time when the tax was impossible of computation?

III.

If there was such a transfer, was it not exempt from the imposition of the tax:

(a) Because of the specific exemption of Section 1802(b)(1) of the Internal Revenue Code, and

(b) Because of the recognized rule that doubtful or ambiguous tax regulations will be construed most strongly in favor of the taxpayer?

REASONS RELIED UPON FOR ALLOWANCE OF THE WRIT.

1. The Eighth Circuit Court of Appeals has ruled that when a custodian, who held the assets of Petitioner as required by law, purchased securities on behalf of Petitioner with the funds of Petitioner, there was a transfer of Petitioner's right to receive those securities to the custodian, and in so ruling has decided an important question of Federal law, and such holding is in conflict with applicable decisions of other Courts of Appeals and with prior decisions of the Circuit Court of Appeals for the Eighth Circuit.

Birmingham v. *Central Life Assur. Soc.*, 141 F. 2d 116 (C. C. A. 8th, 1944).

Occidental Life Insurance Co. v. *Rogan*, 141 F. 2d 1011 (C. C. A. 9th, 1944).

Corporation of America v. *McLaughlin*, 100 F. 2d 72 (C. C. A. 9th, 1938).

Orpheum Bldg. Co. v. *Anglim*, 127 F. 2d 478 (C. C. A. 9th, 1942).

2. The Circuit Court of Appeals for the Eighth Circuit has held that the transfer of the right to receive occurred when custodian purchased the securities. In so holding, the Court has ignored the plain meaning and

effect of Petitioner's compliance with the Investment Advisers Act, and has reached a decision in conflict with the decisions of another Circuit Court of Appeals.

Investment Advisers Act (1940), Section 80 **a-17(f).**

Corporation of America v. *McLaughlin*, 100 F. 2d 72 (C. C. A. 9th, 1938).

3. The Court of Appeals has decided that, in failing to "attach" an exemption certificate to the transfer of its right to receive, Petitioner was not eligible for the exemption specifically provided for in the Internal Revenue Code, and in so doing has ignored and refused to apply the rule of construction that doubtful or ambiguous taxing statutes should be construed most favorably to the taxpayer, and has so far ignored the plain meaning and intendment of the applicable statutes and regulations as to call for this court's power of supervision.

Internal Revenue Code, Section 1802(b)(1).

Treasury Regulations 71(D), Section 113(f) (1941).

T. D. 5578, 1947-21, Int. Rev. Bull. 14.

McFeely v. *Commissioner*, 296 U. S. 102, 111, 56 S. Ct. 54, 58, 80 L. Ed. 83, 101 A. L. R. 304.

Crooks v. *Harrelson*, 282 U. S. 55, 61, 51 S. Ct. 49, 51, 75 L. Ed. 156.

Reinecke v. *Gardner*, 277 U. S. 239, 244, 48 S. Ct. 472, 72 L. Ed. 866.

Birmingham v. *Central Life Assur. Co.*, 141 F. 2d 116 (C. C. A. 8th, 1944).

Corporation of America v. *McLaughlin*, 100 F. 2d 72, 74 (C. C. A. 9th, 1938).

Wherefore, your Petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this court directed to the United States Circuit Court of Appeals for the Eighth Circuit commanding said court

to certify and send to this Court a full and complete transcript of the record and of the proceedings of the said United States Circuit Court of Appeals for the Eighth Circuit in the case entitled Dan M. Nee, United States Collector of Internal Revenue for the Sixth District of Missouri, Appellant, vs. United Funds, Inc., a Corporation, Appellee, Docket No. 13654, to the end that this cause may be reviewed; and that the Petitioner be granted such other and further relief in the premises as to the Court may seem appropriate and proper.

United Funds, Inc. (Petitioner),

By _____,

DANIEL L. BRENNER,

Counsel for Petitioner.

ROACH, BRENNER & WIMMELL,
of Kansas City, Missouri,
Of Counsel.

Supreme Court of the United States

OCTOBER TERM, A. D. 1948.

No. _____.

UNITED FUNDS, INC., A CORPORATION,
PETITIONER,

VS.

DAN M. NEE, UNITED STATES COLLECTOR OF INTERNAL REVENUE FOR THE SIXTH DISTRICT OF MISSOURI,
RESPONDENT.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I.

OPINIONS IN THE COURT BELOW.

The opinion of the District Court is reported as 72 F. Supp. 134.

The opinion of the Circuit Court of Appeals for the Eighth Circuit is reported in 169 F. 2d 33, and appears in full in the record (R. 132-145).

II.

STATEMENT OF BASIS ON WHICH THE JURISDICTION OF THIS COURT IS INVOKED.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of June 7, 1934, Chapter 426, 48 Stat. 926 (28 U. S. C. A. 347a).

III.

STATEMENT OF THE CASE.

Petitioner has stated the case in the "Summary statement of the matter involved" in the foregoing petition for writ of certiorari, which is hereby adopted and made a part of the brief.

IV.

SPECIFICATION OF ERRORS INTENDED TO BE URGED.

1. The Circuit Court of Appeals erred in holding that Petitioner transferred its right to receive securities to its Custodian.

2. The Circuit Court of Appeals erred in ruling that the time of the transfer of the right to receive was contemporaneous with the purchase of securities by Custodian.

3. The Circuit Court of Appeals erred in holding that Petitioner was not exempt from the documentary stamp taxes.

4. The Circuit Court of Appeals erred in refusing to apply the rule of construction that doubtful taxing statutes will be construed most strongly in favor of the taxpayer.

V.

ARGUMENT.

POINT A.

Petitioner's appointment of a custodian to receive its assets and securities, as it was required by law to do, did not constitute a transfer of a right to receive which was subject to a documentary stamp tax under the Internal Revenue Code.

Section 80(a)-17(f) of the Investment Advisers Act of 1940 required, for the protection of investors, that Petitioner place and maintain its securities and similar investments with a Custodian. This Petitioner did. The position of the Commissioner is that such required course of procedure nevertheless constituted a taxable transfer of the right to receive legal title to securities.

The only analogous situations of which your Petitioner is aware are those involving the compulsory transfer by insurance companies of securities to state insurance commissioners to protect the value of their policies within the various States. The situations are precisely parallel, a required deposit of securities with a custodian to protect investors. And the ruling of the Eighth Circuit Court of Appeals, as well as other Courts of Appeals, has been that such transfers do not constitute a transfer of legal title or the right to receive legal title, but only a transfer of possession.

In *Birmingham* v. *Central Life Assur. Soc.*, 141 F. 2d 116 (C. C. A. 8th, 1944), the insurance company paid, under protest, a documentary stamp tax on its delivery of bonds to the Iowa Insurance Commissioner. It then instituted suit to recover the taxes so paid. From a District Court judgment for the insurance company Commis-

sioner appealed. The Eighth Circuit Court of Appeals approved the holding of the District Court, saying l. c. 118, 119:

> "The transaction does not involve a sale, an agreement to sell, a memorandum of sale or a delivery or transfer of legal title to the securities deposited. The purpose or intent with which the delivery was made must, therefore, be considered; for it is inconceivable that Congress intended to tax under this section every delivery of bonds, except those enumerated in the provisos, under all circumstances, without regard to the purpose, the intent, or the jural relations of the parties. The single fact that A delivers bonds to B is insufficient to enable either the Commissioner of Internal Revenue or the court to determine whether or not such delivery is taxable under the statute. Some intent or purpose is necessary to give meaning to the delivery. * * * To be taxable under Section 3481 within the meaning of the regulation, the delivery of bonds must at least be with intent to pass title. This is a reasonable construction of the statute, and no reason appears why it should not be applicable in this case. Nothing in the statute or the regulations points to a contrary conclusion. The argument of the Collector that mere physical delivery of the bonds is taxable is inconsistent with the regulation."

Almost contemporaneously with this decision, the Ninth Circuit Court of Appeals reached precisely the same conclusion in *Occidental Life Insurance Co.* v. *Rogan,* 141 F. 2d 1011 (1944).

On the hearing of your Petitioner's case in the District Court (72 F. Supp. 134) the court recognized that the Custodian occupied the same position as the Commissioner of Insurance in *Birmingham* v. *Central Life Assur. Soc., supra,* and upheld Petitioner's contention

that there had been no transfer of the right to receive legal title to securities from Petitioner to its Custodian. And see: *Corporation of America* v. *McLaughlin*, 100 F. 2d 72, 75 (C. C. A. 9th); *Orpheum Bldg. Co.* v. *Anglim*, 127 F. 2d 478 (C. C. A. 9th, 1942).

In determining that Petitioner was liable for a documentary stamp tax as a transferor of a right to receive because of its appointment of a Custodian to hold its securities for the protection of its investors, as it was required by law to do, the Circuit Court of Appeals has reached a conclusion in conflict with its own prior decisions and the decisions of other Circuit Courts of Appeal.

POINT B.

Assuming a transfer of petitioner's right to receive, such transfer was made before the purchase of any securities, and any attempted tax must fail since it would be impossible of computation.

Assuming, without admitting, that there was a transfer of a right to receive legal title from Petitioner to its Custodian, when was such transfer accomplished? Before any securities were purchased, all of Petitioner's funds were transferred to its Custodian under the terms of a "trust" agreement, Custodian selected and registered its nominee, and Custodian notified the brokers that stock was to be issued to the nominee. The transfer must necessarily have occurred upon the completion of these arrangements. The levying of a transfer tax on a transfer of the right to receive from Petitioner to Custodian each time a broker delivered securities to Custodian's nominee (with the broker paying a documentary stamp tax at that time) not only imposes double taxation upon Petitioner, but is in direct contravention of a decision of the Ninth Circuit Court of Appeals. In *Corporation of America* v. *McLaughlin*, 100 F. 2d 72, 74 (1938), it was held:

"So far as concerns the 1,200,000 shares of stock dividends, we assume, for purposes of determining the character of their subsequent issue, that the trustees acquired from the corporation all the shares on which the stock dividends were subsequently declared, by a transfer from third parties of the right to receive such shares. On this assumption the question is, 'Is that transfer of the original shares a transfer also of the right to receive stock dividends not then declared but which may possibly be declared in the future?'

"Such a purpose in the minds of Congress is conceivable, but is open to the objection that the incidence of the tax is not when the stock dividend is distributed but the time of the transfer of the right to receive the stock to which the subsequent dividend is declared. The stamps are to be affixed then, and their amount, if it includes the right to future stock dividends is *impossible of computation* * * *" (Italics added).

POINT C.

The transactions of taxpayer were exempt from stamp taxes under the specific provision of Section 1802(b)(1) of the Internal Revenue Code and the recognized rule of construction that a taxing statute of doubtful intent shall be construed most strongly in favor of the taxpayer.

After the decisions in the Supreme Court that transfers of the right to receive securities were subject to the documentary stamp tax (*Raybestos-Manhattan Corp.* v. *United States*, 296 U. S. 60, 56 S. Ct. 63, 80 L. Ed. 447; *Founders General Co.* v. *Hoey*, 300 U. S. 268, 57 S. Ct. 457, 81 L. Ed. 639), Congress amended Section 1802 of the Internal Revenue Code to specifically exempt owner-custodian transactions:

"Section 1802 * * * (b) * * * The tax shall not be imposed upon deliveries or transfers of shares or certificates—(1) From the owner to a custodian if under

a written agreement between the parties the shares or certificates are to be held or disposed of by such custodian for, and subject at all times to the instructions of the owner; * * *. No exemption shall be granted under this paragraph unless the deliveries or transfers are accompanied by a certificate setting forth such facts as the Commissioner, with the approval of the Secretary, may by regulation prescribe as necessary for the *evidencing of the right to such exemption* * * *" (Emphasis added).

Treasury Regulations 71(d), Section 113(f), 1941, provide for such a certificate to be attached to shares which are transferred in order that they be exempt from the stamp tax.

The Regulation is clearly limited to those instances in which there is a physical transfer of shares, and manifests no requirement that an exemption certificate accompany the ethereal transfer of a right to receive. Giving the regulation the benefit of a most liberal interpretation, without *any* techical refinements in construction it is still no more than doubtful and ambiguous.

The Circuit Court of Appeals ruled that, since provisions granting special tax exemptions are to be strictly construed, the above regulation would be interpreted as requiring that a certificate accompany the transfer of a right to receive from Petitioner to its Custodian in order that such transfer be exempt under Section 1802(b) of the Internal Revenue Code. In so doing, the Court's ruling conflicts with applicable decisions of this court, its own prior decisions, and the decisions of other Circuit Courts of Appeals.

The holding of this same Eighth Circuit Court of Appeals in *Birmingham* v. *Central Life Assur. Co., supra,* is particularly applicable. This case, as previously noted, in-

volved an attempt to impose a documentary stamp tax upon the delivery of bonds by the insurance company to the Iowa Insurance Commissioner. The Collector there requested application of the same rule of construction applied in the instant case. Said the Court (141 F. 2d 116, 119):

> "It is urged further that the provisions of the statute are to be interpreted broadly; that they evidence an intent of Congress to tax every transaction within the reach of their terms; and that those terms are not to be narrowed by technical requirements, citing *Raybestos-Manhattan Co.* v. *United States*, 296 U. S. 60, 56 S. Ct. 63, 80 L. Ed. 44, 102 A. L. R. 111; *Founders General Corp.* v. *Hoey*, 300 U. S. 268, 57 S. Ct. 457, 81 L. Ed. 639, and like cases. It is true that the reach of a taxing act whose purpose is obvious is not to be restricted by technical refinements (296 U. S. 60, 56 S. Ct. 65, 80 L. Ed. 44, 102 A. L. R. 111), or narrowed by technical requirements. It is also true that 'a taxing statute, if of doubtful intent, should be construed favorably to the taxpayer.' *McFeely* v. *Commissioner*, 296 U. S. 102, 111, 56 S. Ct. 54, 58, 80 L. Ed. 83, 101 A. L. R. 304. 'Such statutes are not to be extended by implication beyond the clear import of the language used.' *Crooks* v. *Harrelson*, 282 U. S. 55, 61, 51 S. Ct. 49, 51, 75 L. Ed. 156; *Reinecke* v. *Gardner*, 277 U. S. 239, 244, 48 S. Ct. 472, 72 L. Ed. 866. The statute cannot be construed to include transactions not clearly within the intent of Congress. In the present case an intent to transfer the legal title to the securities to the insurance commissioner is absent * * *." See also *Corporation of America* v. *McLaughlin*, 100 F. 2d 72, 74 (C. C. A. 9th, 1938).

To levy a tax upon a transaction which is specifically exempted from such taxation because an unrequired certificate is not attached to an intangible right to receive ignores the long established rule of construction that doubtful or ambiguous provisions will be construed in

favor of the taxpayer, your Petitioner. The doubtfulness and ambiguity of the Regulation was recognized by the Treasury Department's subsequent amending of Section 113(f) of Treasury Regulation 71(D) (1941) by T. D. 5578, 1947-21, Int. Rev. Bull., 14, to eliminate this defect.

CONCLUSION.

It is respectfully submitted that in upholding the imposition of a second documentary tax stamp upon Petitioner, the Eighth Circuit Court of Appeals has transgressed the decisions of this Court, the decisions of other Circuit Courts of Appeal and its own prior decisions to an extent calling for the exercise by this Court of its supervisory powers by granting a writ of certiorari, and thereafter reviewing and reversing the said decision.

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